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DEPT FOR AF/S/MTABLER-STONE; AF/EPS; EB/IFD/OMA
USDOC FOR 4510/ITA/MAC/AME/OA/DIEMOND
TREASURY FOR OAISA/RALYEA/CUSHMAN
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SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER FEBRUARY 10 2006
ISSUE

11. Summary. Each week, Embassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- December Manufacturing Resumes Growth;
- Survey Shows Slower 2005 SA Employment Growth;
- Net Reserves Reach \$18.7 Billion;
- Growth Initiative Announced;
- January Business Confidence High but Unbalanced;
- November Retail Sales Come in High; and
- Accelerated Land Reform Wanted.

End Summary.

December Manufacturing Resumes Growth

12. As consumer demand remained strong during the holidays, December's manufacturing production showed higher growth at 6.6% (seasonally adjusted, y/y), compared to November's growth of 4.1%. For 2005 as a whole, manufacturing production growth cooled as the rand continued to strengthen albeit at a slower rate compared to 2004. 2005's manufacturing production grew by 3.5% compared to 2004's 4.4% growth. The highest growing sectors were food and beverages and motor vehicle and parts at 6.4% and 11.1% respectively, with basic iron and steel and machinery along with textiles showing declining production of -0.6% and -2.2%, respectively. Table 1 shows yearly manufacturing growth for the past three years.

Table 1.	2003	2004	2005
Manufacturing Production	-1.8%	4.4%	3.5%

Source: Statistics SA Release, P3041.2, February 9.

Survey Shows Slower 2005 SA Employment Growth

13. According to Grant Thornton's 2006 Employment Growth Index (EGI), manufacturing employment declined by 3% in 2005 compared to 2004's growth of 4.5% and accounted for the reduced growth in overall 2005 employment. Employment in the manufacturing sector has shown similar weakness in other recent surveys. According to the Investec Purchasing Managers' index (PMI), the manufacturing sector activity could drop further. The PMI, which measures manufacturers' confidence levels, dropped below the 50 levels for the first time in more than two years in

January. Over the past year, PMI manufacturing employment index has remained consistently below 50, indicating reduced employment levels. On the positive side, other major sectors reported sharp growth in employment. The construction, service and retail sectors reported employment growth of 11%, 6% and 5%, respectively. In 2004, these three sectors showed similar growth. Employment in businesses having between 50 and 250 workers expanded by 3% compared to 2004 and 2003's growth of 6% and 5%, respectively. All major South African cities increased employment, with Cape Town's 6% growth the highest. Durban experienced the lowest growth at 1%. Gauteng reported 2% growth, down from 6% in 2004, and Port Elizabeth and East London were at 3%, compared to the previous year's growth of 11%. The EGI, which forms part of the Grant Thornton 2006 International Business Owners Survey, showed that on balance, 32% of all South African respondents said they expected to increase their staff complement in 2007. Source: Business Report, February 5.

¶4. Comment. The Grant Thornton International Business Owners Survey contacted 7,000 owners of medium sized businesses from 30 countries. In South Africa, 300 business owners who employ between 50 and 250 staff were contacted. End comment.

Net Reserves Reach \$18.7 Billion

¶5. According to the South African Reserve Bank, net reserves rose by \$1.5 billion, reaching \$18.7 billion at the end of January, up from \$17.19 billion at the end of December. Gross reserves increased to \$22.2 billion from \$20.7 billion. Net gold and foreign currency reserves grew by 8.8% reaching levels of \$2.2 and \$19.9 billion,

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respectively, as foreign exchange purchases arising from FDI-related transactions increased. The rand strengthened by 4.7% in January, in response to increased capital flows and high precious metals prices. In January, the rand averaged 6.09 per dollar and the average gold price reached \$571.22 per ounce, an 11% monthly increase. Source: Business Day, February 8.

Growth Initiative Announced

¶6. President Mbeki announced the Accelerated and Shared Growth Initiative of South Africa (ASGISA), and described ASGISA as a limited set of interventions designed to accelerate overall Accelerated and Shared Growth Development whose ultimate goal is to halve unemployment and poverty by 2014. ASGISA focuses on microeconomic reforms to ameliorate the high costs of intermediate inputs and regulatory environment, rather than any change to its overall macroeconomic policies. Deputy President Mlambo-Ngcuka provided more details, emphasizing the shared commitment necessary to achieve sustainable and balanced economic growth. Six economic constraints and selected government interventions designed to accelerate growth were identified. The following constraints were cited: (1) volatility and level of the currency, (2) costs, efficiency and capacity of the national logistics system; (3) shortage of skilled labor; (4) limited competition and new investment opportunities; (5) regulatory environment and its burden on small and medium businesses; and (6) deficiencies in state organization, capacity and leadership. The following types interventions were recommended: (1) improving infrastructure, (2) encouraging certain sectors with priority industries being tourist and business process outsourcing, (3) improving education and skills, (4) developing the second economy, (5) improving public administration; and (6) developing better government budgeting and expenditure management. Most of the

infrastructure projects are aimed at improving the Durban-Gauteng transport corridor, building a wireless broadband network through the parastatal Sentech, and construction of a new dam in Limpopo Province. Source: Business Day, February 7; www.info.gov.za.

January Business Confidence High but Unbalanced

¶7. The January South African Chamber of Business (SACOB)'s Business Confidence Index (BCI) rose to record high level of 131, primarily because of the financial sector's strength. SACOB's BCI contains 13 indices representing economic trends impacting confidence, among which include manufacturing production, liquidations, core inflation, the real prime interest rate, the gold price and the rand exchange rate. According to SACOB, over 90% of the January index improvement was caused by trends and developments in financial markets rather than any real economic activity. Only one financially related index declined in January, while five of the real economic indicators worsened. SACOB fears that the unbalanced nature of business confidence reflects a further unbalanced South African growth. Source: Business Day, February 8.

November Retail Sales Come in High

¶8. South Africa's retail sales accelerated to 8.1% in November, compared to October's increase of 7%, according to Statistics SA. Real quarterly retail sales increased by 6.8% and sales for the first 11 months were up 6.5% y/y. At its February monetary policy committee meeting, the South African Reserve Bank (SARB) listed strong consumer spending and credit demand, as well as higher food inflation and persistently high oil prices, as threats to the inflation outlook. SARB governor Tito Mboweni stated that two of the main risks, oil and food prices, were exogenous, and the Bank was disinclined to react to them unless they had second-round price impacts. Strong consumer demand growth has been a major reason for the above 3% GDP growth over the past several years. The November's surge in retail sales growth reinforces expectations that interest rates will remain unchanged for

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the first half of 2006. Source: Reuters, Business Day and Business Report, February 9.

Accelerated Land Reform Wanted

¶9. President Thabo Mbeki announced in the State of the Union address that the government would review its willing seller, willing buyer approach to land restitution, following both international and domestic legal standards. Tozi Gwanya, chief Land Claims Commissioner, said that government will start procedures to expropriate land from owners where negotiations have lasted more than several years. The South African government estimates that 96% of commercial farmland is owned by whites, making up approximately 10% of the population. The government wants to transfer 30% of commercial farmland to blacks by 2014, but so far less than 4% has been transferred. Settling land claims of those who were forced off their land during the apartheid regime is also a government priority. South Africa has settled 67,000 land claims out of 79,000, although 7,000 rural claimed remain. The government's target of settling all land claims by March 2008 is seen as key to social stability, important for an improved investment climate. (Business Day, February 9)

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